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SUBJECT: Short March: Innovation and IPR in Huizhou -- TCL
Communications and Huizhou University

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REF: A) Guangzhou 11352 and previous, B) 05 Guangzhou 20435
(notal)

¶1. (SBU) Summary: TCL Communications -- part of embattled
color television and cell phone giant TCL and one of the
largest domestic manufacturers of fixed line phone
equipment in China -- is itself struggling to find some
greater room in a highly competitive environment for a
relatively low technology commodity, but it is nevertheless
embarking on further R&D to expand and improve its product
line and taking some steps to protect its intellectual
property rights as well. Afterwards, Huizhou University
students demonstrated their good understanding of the
importance of intellectual property rights (IPR) in
establishing an innovative culture in China. End Summary.

¶2. (SBU) In Huizhou, our way station rest stop on the way
back to Guangzhou from our "short march" to eastern
Guangdong (ref A), we arranged to meet with executives of
color television and cell phone giant TCL -- Huizhou's
largest enterprise and, after merging its color TV
operations with those of France's Thomson, the largest
manufacturer of cathode ray tube sets in the world. We had
previously visited TCL, but senior executives had almost
been "too busy" -- perhaps because the company's fortunes
have not been particularly rosy (ref B). But this time, at
the intercession of municipal authorities, TCL made
available Yuan Yuncheng, Chief Operating Officer of TCL
Corporation. We had also hoped that the meeting would have
been directed at TCL's color television or cell phone
operations, but instead the meeting was at TCL
Communication Equipment, even though the CEO of that branch
company, Gu Gong, also received us.

TCL Communication

¶3. (SBU) Gu said that TCL Communication builds phone
equipment, cell phones, and networking equipment, both
wired and wireless, and the company is the largest
manufacturer of conventional, fixed line phones in China.
This was the original product of the parent corporation,

TCL, and was the basis for TCL's initial rise as a whole. Although TCL Communications' primary market is China, Europe is their main export market. The company is also increasing its presence in Southeast Asia and India.

From Traditional To the Newfangled

¶4. (SBU) Gu noted that despite its dominant domestic market share, TCL Communications is in a tough competitive environment because its products have largely been commoditized. To meet the challenge of that environment, the company has recently broadened the types of products it manufactures, including VOIP phones, ADSL and WLAN equipment, and a fixed line CDMA-compatible phone. The company is shifting its focus on developing the broadband and wireless markets and moving away from the cutthroat low margin industry of conventional phones, of which 85% are built in China.

IPR Even For Commodities

¶5. (SBU) Knowing that a focus of the Consulate during the "short march" was on IPR, Gu noted that the company has had problems with inferior copies of their phones being sold at lower prices by counterfeiters. TCL Communication now employs an IPR department and a law firm to enforce its IPR. Parent company COO Yuan added that IPR problems for TCL were not limited to the fixed line phone company division alone but extended to the company as a whole, and TCL aggressively pursues the protection of its interests. (Huizhou Science and Technology Bureau Deputy Director and IP Office Director Chen Tian, who accompanied us to TCL and who participated in a separate meeting with Huizhou Secretary General Ye Zexiong, told us that because Huizhou

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GUANGZHOU 00011568 002 OF 003

is the home base to many major Chinese and foreign-invested consumer electronics firms, the city and its business associations were very active in brand protection and seeking to root out counterfeiters, including those from other areas in China.)

TCL Needs to Innovate

¶6. (SBU) COO Yuan turned the conversation to the need for TCL as a whole to continue improving its products in order to compete in a very challenging market place. In that respect, it has enhanced its research facilities in Chengdu and Xi'an due to the high quality engineering universities located in those cities. TCL's engineers and researchers are predominantly Chinese and fairly young (under 30 years old), most going directly to TCL after graduation. There are few engineers and researchers with previous work experience, especially work experience in foreign companies or overseas. Yuan introduced Liu Bingyun, a Vice General Engineer of the parent company and the General Manager of the R&D Center for TCL Communications, as typical of the quality staff that the company has hired to spur further innovation.

Envisioning the Future

¶7. (SBU) In response to a question about whether TCL, like some U.S. high technology firms, has "skunk works" or "brainstorming mosh pits" to come up with new ideas or products, Yuan said that the TCL company encouraged a lot of interaction between the R&D centers and the production and marketing offices. Asked about a TCL vision of the future of consumer electronics, Yuan said he envisioned one in which consumers who traveled frequently would seek a small, single multi-functional device incorporating phone, messaging, e-mail, web-browsing, photography, and audio video but at the same time, homes would feature much larger standalone devices -- personal computer, phones, cameras,

televisions, and/or home entertainment systems. Yuan expressed confidence that TCL would play a role in manufacturing products for such markets.

Comment on TCL

18. (SBU) In Guangzhou's "Tele Tale Harts" message (ref B), we assessed the prospects for three south China consumer electronics companies adopting different strategies for success -- TCL as a Samsung wannabe competitive across all product categories, XOCECO wanting to be a mini-Sharp focused solely on high-end products such as flat panel televisions, and upstart Amoi focused on being, well, upstart and full of buzz in its products. Of the three, TCL, with its bumpy joint ventures with Thomson (in the increasingly obsolescent production of cathode ray tube (CRT) color televisions) and Alcatel (in cell phones and other telecoms products), has been the big fizzler, losing RMB 692 million (US\$ 86.5 million) in 2005 compared to a RMB 373 million (US\$ 46.2 million) net profit in 2004. Still, the company is still scrappy and enjoys a lot of support from both Huizhou and provincial authorities. Unfortunately, such support doesn't translate directly into product sales, especially since TCL faces huge competition in every one of its product categories.

Huizhou University Students

19. (SBU) At Huizhou University, an audience of 250 students enthusiastically commented on Congenoffs presentations on IPR and American innovation culture. They clearly drew the connection between the notion that IPR violations constituted theft and could have far reaching safety and other consequences, although there continued to be arguments that watching illegal DVDs was all right in the absence of genuine products or that China needed an opportunity to catch up in IP before a more effective enforcement regime could be put into place. On innovation, audience members clearly understood that the successful American experience was one of incredible dynamism (in being able, for example, to discard outmoded ways of doing

GUANGZHOU 00011568 003 OF 003

things without hindrance by entrenched interests potentially hurt by rapid change) and diversity and openness -- with many students wishing that China could follow a similar path.

Looking Ahead to the "Long March"

10. (SBU) This is last of Consulate Guangzhou's "short march" messages, and soon we will be transmitting our series on cities visited during our "long march" into the Hakka and Minnan "heartlands" in northeastern Guangdong and southwestern Fujian Provinces.

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